

**THE QUESTION OF SECURE U.S.
MARKET ACCESS IN THE CANADA-U.S.
FREE TRADE AGREEMENT**

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GOVERNMENT OF ONTARIO

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EXECUTIVE SUMMARY

Canadian producers rely heavily upon export markets, and the importance of the U.S. market to Canadian exporters has grown substantially over the last few decades.

International trade liberalization in general, and secure access into the U.S. market in particular, are important to ensure continued growth for the Canadian economy.

The rapidly changing structure of international competition for export markets, the decreasing importance of the import tariff as a tool for domestic market protection, and the substantial U.S. trade deficit, have all led to an increased use of trade remedy laws by U.S. producers and the U.S. government since 1980.

An examination of previous cases shows that the use of U.S. trade remedy laws by American-based producers has adversely and disproportionately affected Canadian exports such as natural resources, agriculture, and certain manufactured and steel products. These trade actions (e.g., softwood lumber, fish, potash) have implications for regional economies.

The threat or use of U.S. trade laws can influence the investment decisions of domestic and foreign investors, especially whether to newly invest or expand on present production facilities in either Canada or the U.S.

The Canadian Federal government initiated trade discussions with the U.S. in order to achieve the principal objective of secure access for Canadian exports into the U.S.

A market access evaluation of the Canada-U.S. Trade Agreement, as signed on January 2nd, 1988, indicates that:

- i) while overall U.S. market access for Canadian exports is enhanced through U.S. tariff reductions, there appears to be little gain of new market access into the important U.S. government procurement markets.
- ii) as to the principal goal of secure U.S. market access, there appears to be little change from the status quo. Neither the present rules governing

antidumping (AD) and subsidy/countervail (CVD) investigations nor the administering bodies are affected in any way by the Agreement. The new binational dispute settlement Panel for these cases, while potentially advantageous in that it might accelerate the present judicial review process, does not possess any increased power or differing review mandate than the present system. With the exception of safeguard measures, all other U.S. trade remedy laws are not affected by the Agreement.

- iii) it is not clear that enshrined U.S. market access was achieved. Retaliation as a remedy in instances of non-compliance does not reflect the relative political and economic disparities between the two countries. Moreover, there are serious concerns over the degree of allowable provincial involvement in the resolution of bilateral disputes, particularly whenever such bilateral disputes involve areas of provincial responsibilities.

Overall, the inability of the Agreement to secure meaningfully U.S. market access in effect maintains the present vulnerability of Canadian exports to U.S. trade remedy laws, and would not appear to reduce it in future.

For Canadian-based companies the increased level of access into the U.S. market resulting from the Canada-U.S. Trade Agreement would largely be due to U.S. tariff elimination. The potential economic benefits from this increased level of access, however, could be offset by trade remedy actions that prevent Canadian industries from competing effectively in the U.S.

This lack of secure U.S. market access would appear to make vulnerable the corporate strategies of Canadian-based companies aiming to benefit from any increased U.S. market access that would result from the Agreement. As well, potential government programs and policies which attempt to facilitate needed private sector restructuring and adjustment to current changes in multilateral and bilateral trade patterns and sources of competition would remain vulnerable to U.S. trade actions.

The Agreement does not provide Canada with an exemption from future changes to most U.S. trade laws. The value of the limited exemption from future changes in U.S. AD and CVD laws is dramatically curtailed by the absence of an effective enforcement mechanism.

The U.S. Omnibus Trade Bill, recently passed by the U.S. Congress, serves as an example of the inability of the Canada-U.S. Trade Agreement to protect Canada from either present or future changes in U.S. trade laws. As such, it highlights the inadequacy of the market access provisions in the Agreement.

Planned future negotiations to develop new bilateral rules and procedures governing AD and CVD investigations would likely, if successful, require further concessions by Canada in the form of constraints on government industrial and regional development programming. Given the costs of abrogation of the Agreement for Canada, Canadian negotiators would not be in a strong bargaining position in these negotiations.

U.S. industry interests are attempting to maintain protection under the Agreement through inclusion of the threat of AD/CVD and self-initiated Section 301 actions in U.S. legislation implementing the Agreement.

The fact that the negotiations did not meaningfully change bilateral trade remedy laws or their application, should be seen as a significant shortcoming of the Agreement in balancing the overall gains and concessions in the broader Canada-U.S. trade negotiations. The inability of the Agreement to ensure secure U.S. market access in turn places greater importance in the need for Canada to pursue trade expansion and liberalization on a global basis.

I INTRODUCTION

The United States is Canada's number one export market. Canada's exports to the U.S. have been rising steadily as a percentage of total exports for the last few decades, and have more than doubled in value in the last ten years (see Tables A-1 & A-2 in Appendix A). As a result, U.S. protectionism in the form of possible trade actions against imports, which threatens or reduces Canadian exporters' access to the U.S. market, could represent a major economic threat to Canada.

The Canadian government responded to this potential threat by initiating the negotiation of a bilateral Trade Agreement ("Agreement") with the U.S. While the objectives stated by the Federal Government¹ were to secure, enhance and enshrine Canada's access into the U.S. market, Canada's key objective was to achieve secure market access. How well this key objective was achieved can be viewed as a measure of the value of the Agreement which was signed on January 2, 1988. The purpose of this paper is to examine the extent to which the Agreement provides Canada with a significant improvement in secured U.S. market access. Any gains to Canada in this area would also have to be weighed against the costs to Canada of concessions in other areas under negotiation in order to reach an overall assessment of the Agreement.

It is important to keep in mind that Canada has substantially higher tariffs than the U.S. The elimination of these tariffs, without assured access to the U.S. market, could have serious implications for the future ability of Canadian industries to compete, through the proposed Agreement, in both the Canadian and U.S. markets. U.S. imports into Canada would increase, putting strong competitive pressure on Canadian producers in the domestic market. At the same time, however, Canadian producers could be limited, by the continued application of U.S. trade remedy laws, in their ability to improve their competitiveness through increased exports to the U.S.

The central question is how beneficial reduced U.S. tariff barriers would be for Canada if any increased access to the U.S. market gained under the Agreement can be countered by trade actions -- or threats of actions -- against competitive Canadian exports.

¹See "Canadian Trade Negotiations: Introduction, Selected Documents, Further Reading"; prepared by the Department of External Affairs, December 15, 1985.

II U.S. TRADE REMEDY LAWS

A. Trade Liberalization and the Use of Contingency Protection

It is generally recognized that Canada has an open economy which relies heavily upon international trade. Liberalized international trade is more important to Canada than it is to many countries that are commonly thought of as world trading powers, such as the U.S. and Japan. Canada's total merchandise exports account for 28% of GNP with exports to the U.S. accounting for about 22% of GNP. Only 13% of Japan's GNP and 7% of the U.S. GNP is accounted for by exports (see Appendix A). Because of this, international barriers to trade and conversely trade liberalization tend to have a proportionately greater impact on Canadian production than is the case for our main trading partners.

A recognition of the importance of liberalized international trade to global economic growth was a prime motivating factor behind the formation of the General Agreement on Tariffs and Trade (GATT) after World War II. Canada, along with all other western industrialized countries and a growing number of newly industrializing countries, are all signatories to the GATT. The early work of GATT focused on coordinating a balanced approach to multilateral tariff barrier reductions.

However, the resulting increase of international competition in domestic markets generated substantial pressures for the erection of a multitude of non-tariff barriers (NTBs). Along with this proliferation in the use of NTBs -- such as the use by the U.S. of voluntary restraint agreements (VRAs) on autos, and orderly market arrangements (OMAs) on steel -- industries of GATT signatories have more recently recognized the potential for domestic market protection from foreign competition through the active use of trade remedy laws largely sanctioned by GATT.

Thus, a growing concern to the GATT system has been not only the use of restrictive measures not sanctioned directly by GATT (e.g., VRAs and OMAs), but also the increasing use of contingency protection² measures by individual member nations to restrict trade flows.

²Contingency protection measures is a collective term which refers to anti-dumping (AD), countervailing duty (CVD), safeguards laws and provisions against "unfair trade" practices. These are trade remedy actions, some of which are permitted by the GATT under certain circumstances.

Under GATT Article VI, contingency protection measures, such as AD and CVD, may be brought against imports which, because of the dumping or the subsidization of the product, are found to be causing or threatening "material injury" to a domestic industry. Similarly, safeguard actions may be brought under Article XIX of GATT against fairly traded goods, if a product is being brought into a market in such increasing quantities to cause or threaten "serious injury"³ to domestic producers.

Both Canada and the United States have in place GATT-sanctioned systems of trade remedy laws, although there are some significant differences in rules and procedures. However, given the significance of exports for the majority of Canadian producers (average export propensity for manufactures of over 32%⁴) the use of foreign trade remedy laws against Canadian exports is of considerable importance. In contrast, U.S. producers are largely not export dependent, and the use of Canadian trade laws against U.S. exports (primarily anti-dumping) is seen simply as an additional cost of doing business in Canada.

Of particular concern to Canada has been the increased use since 1980 of trade remedy laws by the U.S. against Canadian products. This increased reliance by U.S. industries on trade remedy laws, as a form of domestic market protection, can be linked to evidence of a loss of competitiveness in certain U.S. sectors, and a resulting increase in the U.S. merchandise trade deficit.⁵

The U.S. Trade Agreements Act of 1979 codified into U.S. trade law the results of the Tokyo Round of multilateral trade negotiations under the GATT. This Act covers the procedures and criteria which the particular U.S. administering authorities follow in interpreting and applying U.S. trade remedy laws. The U.S. administering

³In instances where a product of a GATT signatory is considered to be traded fairly -- there is no evidence of dumping or subsidization -- the GATT required injury test must meet the higher (i.e., serious) injury level than would be the case for unfairly traded goods (i.e., material injury).

⁴See Table 3 on page 14.

⁵See Global Competition: The New Reality, 1985, prepared by the U.S. President's Commission on International Competitiveness.

authorities are the U.S. International Trade Commission (ITC), and the International Trade Administration (ITA) of the U.S. Department of Commerce.

Although these new procedures did not come into play until 1980/81, the actual record of total investigations initiated indicates their substantial use by U.S. producers, (see Table 1).

TABLE 1⁶
RECORD OF TOTAL INVESTIGATIONS INITIATED AGAINST ALL
COUNTRIES UNDER SELECTED U.S. TRADE REMEDY LAWS

YEAR	AD	CVD	Sec.201	Sec.301	Sec.337
1981	19	14	1	5	18
1982	71	124	1	12	23
1983	51	31	2	5	43
1984	73	53	5	3	33
1985	46	29	3	5	25
1986	68	28	2	6	24

A further concern for Canada in the American use of trade remedy laws is that even when the primary sources of international competitive pressure affecting American industries are third countries, Canadian exports can nevertheless be adversely affected.

⁶Source: Information Offices of the U.S. ITC and the Department of Commerce. These selected U.S. trade remedy laws are further defined in Section II(b) of this paper.

Commenting on the U.S. contingency protection system, a senior Canadian Government trade official, noted that:

"Potentially much more distortive than tariffs, this system undermines investment and production planning in a way that the transparent and predictable tariff never could. ...A private U.S. citizen can invoke a variety of different actions to seek redress against the practices of foreign governments and business and to limit import competition. As a result of: 1) low thresholds required to trigger investigations; 2) procedures tending to favour complainants; and 3) lax standards for finding the existence of 'unfair' trade practices; measures to counteract such practices have in themselves become barriers to trade."⁷

It was for this reason that obtaining special treatment under U.S. trade remedy laws in a bilateral Trade Agreement with the U.S. was considered to be a vital objective for the Canadian government.

The importance of this objective is reflected in comments made by both Prime Minister Brian Mulroney and Ambassador Simon Reisman, Canada's chief negotiator in the Canada-U.S. trade discussions. In March of 1987, during a House of Commons debate on the Canada-U.S. trade negotiations, Canada's Prime Minister noted that:

"Our highest priority is to have an agreement that ends the threat to Canadian industry from U.S. protectionists who harass and restrict our exports through misuse of U.S. trade remedy laws."⁸

That same month, Ambassador Reisman also noted the importance of obtaining restrictions over the application of U.S. contingency protection measures:

"Any agreement which did not restrict the use of U.S. dumping and countervail statutes...would not be worth the powder it would take to blow it to hell."⁹

⁷Michael Hart, Trade Remedy Law and the Canada-United States Trade Negotiations, presented at the American Bar Association National Institute Conference on the U.S.-Canada FTA, January 28-29, 1988, pp. 274-275

⁸Prime Minister Brian Mulroney, quoted in The Toronto Star, October 5, 1987.

⁹From an article in The Globe and Mail, March 16, 1987, quoting Ambassador Reisman.

B. Current U.S. Trade Remedy Laws

American contingency protection measures which have allowed the U.S. to initiate trade actions against Canada are sections of the Tariff Act of 1930 as amended by the Trade Act of 1974, the Trade Expansion Act of 1962, the Trade Agreements Act of 1979, and the Trade and Tariff Act of 1984. The sections of U.S. trade remedy laws that are of major concern in regard to U.S. market access are:

1. Title VII - Countervailing Duty and Anti-dumping;
2. Section 201 - Escape Clause (Safeguards);
3. Section 301 - Removing Foreign Barriers;
4. Section 337 - Unfair Practices in Import Trade;
5. Section 232 - National Security Protection.

Under the proposed Canada-U.S. Trade Agreement, American industries would be free to continue to initiate cases against Canadian exports through all sections of U.S. trade remedy law identified above. Only under certain circumstances -- further discussed in this paper -- would the rules governing some of these trade measures be changed as a result of the proposed Agreement. Therefore, existing U.S. trade remedy laws need to be carefully examined as to how they have affected Canadian exports in the recent past.

a) Countervailing Duties (CVD)

Under U.S. law, imported goods are subject to a countervailing duty when it is determined that they have benefited from a subsidy, and cause or threaten material injury to a U.S. industry or materially retard its establishment. When these two conditions are met the imported articles may then be subject to a countervailing duty equal to the amount of the estimated subsidy.

The U.S. definition of a countervailable subsidy covers the provision by government of: capital grants, loans and loan guarantees on terms inconsistent with commercial considerations; the provision of goods and services at preferential terms on a non-commercially justifiable basis; as well as the granting of funds, forgiving of debts to cover operating losses, or the assumption of any costs or expenses in the manufacture, production or distribution of an article.¹⁰

In the U.S., countervailing duty actions have become an increasingly favored trade remedy response to import competition. Products affected by the 13 U.S. CVD cases brought against Canada since 1980 (see Appendix B) tend to be agricultural, fish, resources or steel related. These are products in which Canada would appear to have a clear comparative advantage or where the U.S. industry is uncompetitive.

The United States has particularly focused on natural resource programs and policies utilized by the federal and provincial governments in Canada. For example, provincial softwood lumber stumpage pricing systems were the subject of two countervailing duty actions primarily because they differ from the system used in the United States. Although the initial investigation had exonerated these provincial practices, the Government of Canada negotiated a settlement to end the second investigation following a preliminary U.S. finding that Canadian lumber production was subsidized. The settlement resulted in the unilateral imposition by Canada of a 15% export tax on Canadian softwood lumber products exported to the U.S.

In contrast with the thirteen U.S. CVD actions against Canadian industries since 1980, there has only been one Canadian CVD action against a U.S. industry. This case, the only countervail investigation brought against the U.S. by one of its trading partners, was a recent action which Ontario's corn growers took against U.S. corn imports. The Canadian Import Tribunal determined that subsidized U.S. corn imported into Canada resulted in injury to Ontario producers, and imposed a countervailing duty on U.S. corn imports into Canada.

¹⁰In addition, "upstream subsidies" on inputs to the article in question can be subject to a countervailing duty where they confer a competitive benefit, and have a significant effect in the cost of production.

b) Anti-Dumping Actions (AD)

Under U.S. law, imported goods are subject to antidumping duties where it is determined that they have been sold in the U.S. market at less than "fair value", and cause or threaten material injury to a U.S. industry or materially retard its establishment. Again, if these two conditions are met, an imported product may be subject to an antidumping duty equal to the margin of dumping.

The U.S. law's determination of dumping hinges on the definition of what is the "fair value" of a product. Fair value is determined by the "foreign value", or a "constructed value" of the product which differs substantially from normal accounting based determinations of the cost of production.¹¹ Dumping is then considered to have occurred if a margin between the import price and the "fair value" exists. This margin can be as small as 0.5 per cent. Unlike Canadian rules, constructed value is used frequently, placing a considerable upward bias relative to the actual price of the product in the exporter's domestic market. This results in increased findings of dumping and margins of dumping.

An Ontario government study, prepared by Professor Fred Lazar of York University¹², shows that Canadian companies rarely dumped intentionally, and if the U.S. authorities had used slightly different means of measuring fair value, then little if any dumping margin would have been found in many cases. In addition, rapid currency exchange rate fluctuations may also act as a contributing factor to positive dumping determinations in some instances.

¹¹Constructed value is defined as the sum of costs of production and packaging for shipment to the U.S., and must include general expenses of not less than 10% of direct costs, and a profit margin of not less than 8% of total costs. These minimum margins are likely overestimates of the actual margins which many companies must work with during periods of low product demand and intense price competition.

¹²See: Fred Lazar, Antidumping issues in the Free Trade Negotiations, August 1987, pp. 16-23.

An example of a situation involving these factors was the 1986 U.S. AD case which affected Canadian iron construction castings. In reviewing this case, Professor Lazar noted that:

"...if Canadian companies did dump into the U.S. market, they did so in order to maintain their share of the market in the face of extensive competition, especially from other countries. More likely, the depreciation of the Canadian dollar resulted in price changes in the U.S. market that were inadvertently interpreted by the Department of Commerce as dumping."

As Appendix C points out, several other cases against semi-manufactured metals from Canada have affected substantial volumes of Canadian exports. Also, a recent U.S. antidumping case involved the export of colour picture tubes made by Mitsubishi Canada Inc. In this case, it would appear that the action was primarily aimed at exports from Japan, with the Canadian operation only assessed a dumping margin of 0.65%. As well, a recent and similar U.S. AD case involves computer micro disks from Japan. The U.S. Department of Commerce has yet to determine whether indirect imports from Japan via third countries should continue to be covered by the investigation. This case is of concern to Canada because a Canadian company (Kao-Didak) recently began production and export of such micro disks using inputs from Japan.

The recent U.S. AD action against Saskatchewan potash, on the other hand, is an example of how Canadian natural resource exports, with substantial comparative advantage over U.S. competition, are affected by American trade remedy laws. The AD action was initiated because the U.S. potash industry could not compete with the higher grade Canadian mines as prices fell during a period of declining demand.

In the potash case, the U.S. Department of Commerce announced preliminary dumping margins ranging from 9% to 85% against Canadian producers. The margins and their variance reflect the increasing emphasis on considering "production costs" when determining dumping. Since potash is a fairly homogeneous commodity, sold largely on the basis of price, Canadian producers' selling prices were roughly the same. The variance in the margins determined, therefore, resulted primarily from the measurement of "constructed costs".

c) Safeguard Actions (Section 201)

As previously mentioned, "escape clause" or safeguard actions are permitted under the GATT to protect a domestic industry from increases in competing imports of fairly traded goods, which cause or threaten to cause serious injury to a domestic industry. The U.S. system provides for affected American industries to directly petition for an investigation. Currently, the U.S. President can determine whether or not to provide relief. Such relief can be provided through tariff or quota protection, or domestic adjustment assistance.

An example on the use of this U.S. trade remedy law was the imposition of a 35% import duty in late 1986 on Canadian exports of red cedar shakes and shingles. In this case, the surge of the more competitive Canadian imports into the U.S. market was primarily a function of substantially increased demand in the U.S. for the product, which resulted from a residential construction boom in the U.S. However, the bulk of cases affecting Canada (see Appendix C-1) involve actions aimed primarily at other countries.

d) Removing Foreign Barriers (Section 301)

In contrast to other trade remedy laws, Sec.301 does not deal with restricting imports per se. Rather, it addresses the trade practices of foreign governments, including barriers which are perceived to exist for U.S. goods or services in export markets. Sec.301 allows the President to take action against any foreign government practice which is deemed to be inconsistent with a trade agreement or denies the benefits from an agreement. That is, if the foreign practice is considered to be "...unjustifiable, unreasonable or discriminatory and burdens or restricts United States commerce." "Unreasonable" in this context means practices that are considered "unfair and inequitable". In many cases, these terms are used to describe practices which are legal under international law, but which act to deny U.S. enterprises foreign market opportunities or opportunities for establishing an enterprise in a foreign market.

The U.S. President has discretionary authority in the type of action he can take under Sec.301, including suspending trade agreement concessions, imposing restrictions on imports, or limiting foreign service suppliers access to the U.S. market. The most noteworthy use of this statute for Canada was a Sec.301 investigation in 1978 into Canadian tax policies on transborder broadcasting, and the subsequent U.S. enactment of mirror (i.e., reciprocal) U.S. legislation.

Proposed changes to Sec.301 in the U.S. Omnibus Trade Bill would encourage the Administration to initiate actions more frequently, give private parties greater power to compel action and tighten definitions of "unfair" practices.

e) Unfair Practices in Import Trade (Section 337)

An American trade remedy law which has not been authorized by GATT, is Sec.337 of the U.S. Tariff Act of 1930. The European Community and Canada have recently sought a GATT Panel investigation as to whether Sec.337 is consistent with U.S. GATT obligations. Canada does not have a similar law.

Sec.337 covers imported products which are alleged to benefit from "unfair methods of competition and unfair acts". This law authorizes the U.S. ITC to prohibit the importation of the products in question, when such products substantially injure an efficient and economically operated U.S. industry. This section generally has been utilized in relation to disputes over intellectual property rights, primarily infringement of patents.

The importance of Sec.337 must be stressed. In 1987 (January to November) alone, 22 of the 58 unfair trade complaints investigated by the ITC involved Sec.337. These are primarily aimed against small manufactured goods. Several Canadian products are currently subject to Sec.337 investigation.

f) National Security Protection (Section 232)

Under GATT Article XXI, countries are permitted to take certain actions which they consider necessary for the protection of their essential security interests.

The U.S. utilizes Sec.232 of the Trade Expansion Act of 1962 to limit imports, through Presidential discretion, on national security grounds. Under this Section, the Department of Commerce must determine whether an article "...is being imported into the United States in such quantities or under such circumstances as to threaten to impair the national security". As such, there is no requirement to prove that a U.S. industry has been, or might be injured as a result of the particular imports. This makes the use of this trade law very attractive to many American industries.

Although Sec.232 has in the past mainly been used in relation to strategic materials, it can conceivably be used to limit imports of a wide variety of products. Currently, the U.S. Department of Commerce is investigating three Sec.232 cases potentially affecting Canadian exports. One is targetted against imports of crude oil and refined petroleum products, the second case is looking at imports of anti-friction bearings and the third is against plastics injection moulding machinery.

III IMPLICATIONS OF CURRENT U.S. TRADE REMEDY LAWS FOR CANADA

A. Trade Implications for Canada

The record of bilateral AD/CVD and safeguard measures between Canada and the U.S. from 1980 to mid-1987 is presented below:

TABLE 2¹³
RECORD OF BILATERAL CONTINGENCY PROTECTION MEASURES

Contingency Protection Measures	Measures taken by Canada		Measures taken by the U.S.	
	No. of Cases	Value of imports from US in 1986 (\$ mill.)	No. of Cases	Value of exports to US in 1986 (\$ mill.)
<u>CVD cases</u>				
Investigations	1		11	
Action taken	1	9	6	4,172
<u>AD cases</u>				
Investigations	41		20	
Action taken	23	375	9	295
<u>Safeguard cases</u>				
Investigations	2		13	
Action taken	2	19	4	1,758
<u>Total cases</u>				
Investigations	44		44	
Action taken	26	403	19	6,225

The \$6.2 billion worth of Canadian merchandise exports to the U.S. identified by the Federal Government as being subject to these particular U.S. trade measures represents about 6.7% of total Canadian goods exports to the U.S. in 1986. Professor Rugman, for the year 1983, identifies an even higher proportion (25%) of

¹³Source: Canadian Federal Department of Finance, The Canada-U.S. Free Trade Agreement: An Economic Assessment, January 1988, pp. 22. Note: the softwood lumber CVD case technically involved an export tax imposed by Canada in response to the threatened imposition by the U.S. of a countervailing duty.

Canadian exports that were subject to U.S. CVD, AD and safeguard actions.¹⁴ These numbers indicate that a significant value of exports have been threatened by U.S. trade actions.

Given the high proportion of Canadian domestic production aimed at export markets in general (and the U.S. market in particular), U.S. trade actions have the potential to affect domestic levels of production. The greatest levels of export propensities (see Table 3) are found in the rationalized industries (transportation equip., machinery), and in natural resources and resource-based manufacturing (wood, paper, primary metal).

TABLE 3
IMPORTANCE OF EXPORTS TO THE U.S. FOR CANADIAN
MANUFACTURING INDUSTRIES, 1986

Manufacturing Industries	Total Export Dependence (Total Exports/Shipments)	Export Orientation to the U.S. (Exports to U.S./Shipments)
Food	14.85%	8.36%
Beverage	10.46%	9.98%
Tobacco Products	7.03%	2.06%
Rubber Products	35.64%	33.28%
Plastic Products	16.99%	15.31%
Leather and Allied	9.90%	8.70%
Primary Textiles	13.17%	6.68%
Textile Products	7.08%	5.27%
Clothing Industries	6.86%	5.79%
Wood Industries	52.03%	42.03%
Furniture and Fixtures	22.57%	21.54%
Paper and Allied Products	58.48%	41.70%
Printing & Publishing	6.21%	5.82%
Primary Metal Industries	56.79%	45.57%
Fabricated Metal Products	21.22%	14.41%
Machinery Industries	55.87%	41.26%
Transportation Equipment	89.00%	84.39%
Electrical & Electronic	44.26%	34.44%
Non-Metallic Mineral	12.70%	12.03%
Refined Petroleum & Coal	7.00%	6.48%
Chemical & Chem. Prod.	25.42%	16.67%
Other Manufacturing	45.64%	33.48%
Total Manufacturing	39.15%	32.42%

Source: Canadian Department of Regional Industrial Expansion

¹⁴See Alan Rugman, *Policy Options*, November 1986, pp.22-26.

Not only do these U.S. contingency protection measures affect a significant proportion of Canadian exports to the U.S., but they can also be used by U.S. producers to target protection for their specific industries. As Professor Alan Rugman has noted:

"Another result of U.S. trade law is that it can be viewed by American producers to reinforce discrimination against a single industry. For example, in the ITC Annual Report for 1983 it is stated that of the 57 completed countervailing duty cases, 48 involved steel products; of the 76 dumping cases, 37 were for steel products."¹⁵

This ability to target specific industries for U.S. domestic market protection, can have a disproportionate impact on the various regions of Canada which, due to their less diversified economies, tend to be more exposed to actions taken against key export products.

For example, the success of the CVD petition against fresh Atlantic Canada groundfish affected from 5% to 10% of that region's fish exports. In fact, Rugman¹⁶ has estimated that the impact of U.S. trade law on Atlantic Canada has been to threaten roughly 60% of the region's exports.

A similar case can be made with the Western Canadian provinces where, for example, the recent U.S. safeguard trade action on shakes and shingles and the CVD case on softwood lumber targetted B.C.'s forestry products industries, which account for roughly 50% of the province's goods output.

U.S. trade remedy laws are capable of affecting the export potential of Canada's various regions and industrial sectors. This capability is further compounded when a certain set of economic conditions come into play. For instance, the inherent cyclical pricing conditions which affect most, if not all, natural resource commodities can and does lead to such Canadian exports being particularly vulnerable to AD actions.

¹⁵Ibid.

¹⁶Ibid.

As well, rapid exchange rate fluctuations which in the short-term distort domestic and export price relationships, can also lead to trade actions against a wide range of products. In times of volatile exchange rate market conditions, natural resource exporters face the potential of a double-edged sword in U.S. trade remedy laws. If the export market price is lower than the domestic price or constructed value for the resource, the product is vulnerable to AD action. However, if the price relationship between export and domestic markets is reversed, there is the potential for a CVD action that claims government subsidization of the "downstream" product which incorporates the particular resource.

Moreover, different rates of resource depletion, partly caused by differing domestic resource pricing and extraction policies, can lead to countervailing duty actions such as the recent U.S. investigations against Canadian softwood lumber and groundfish. In fact, the inherently differing philosophies between Canada and the U.S. concerning government's role in economic development -- and the resulting associated programs -- increase the potential vulnerability of Canadian natural resource exports to U.S. claims of Canadian subsidization.

B. Potential Investment Implications for Canada

Canada is viewed as a stable and remunerative location for investment in terms of economic and market growth, expected profitability, political stability and technological and managerial expertise.¹⁷ Moreover, Canada's close proximity to the large and wealthy U.S. consumer and industrial markets has been a strong source of attraction for third country investment.

While many such factors work together to pull investment to domestic industries, the particular attractiveness of the Canadian economy results primarily from: competitive labour costs within North America; well developed transportation links both within Canada and to the U.S.; a highly educated and skilled labour force; a stable social environment; and more recently, a favorable exchange rate.

However, undermining Canada's attractiveness for investors, whether domestic or foreign, is the potentially negative impact that U.S. trade remedy laws have on

¹⁷See Competitiveness Criteria 1987, by the World Economic Forum, Geneva, Switzerland.

important investment decisions.

Given the high proportion of Canadian domestic production which is aimed at the U.S. market compared with the case for U.S. production exported to Canada, there is an implicit asymmetry to the potential for economic costs and related uncertainty in the bilateral use of trade remedy laws that works to Canada's disadvantage. Indications are that U.S. trade remedy laws tend to further increase the level of uncertainty in the production decisions faced by Canadian-based producers. The potential for reduced investment resulting from the uncertainty generated by U.S. trade protection has been recognized.

A Conference Board of Canada survey¹⁸, published in April 1984, attempted to elicit views on Canada's attractiveness as a host country for investment. While noting that criteria related to market factors or corporate policy play a governing role on investment decisions, the survey noted that trade barriers appeared to have had a significant role in recent Canadian investment in the U.S., and its importance seems to be increasing. In as much as the active use of U.S. trade remedy laws is now being recognized as a more recent form of a barrier to trade, their potential impacts on investment decisions might very well be as detrimental as the more conventional NTBs.

Mr. Reisman, in discussing the pros and cons of a bilateral trade deal, noted the uncertainty and associated investment implications for Canada due to U.S. trade remedy laws:

"Still another objection to a free-trade agreement is that it would be dangerous to embark on major new investments geared to the U.S. market in the face of actual or potential non-tariff barriers and actual or potential contingency protection, such as antidumping regulations, countervailing measures, or other emergency import restrictions. This is not a hollow concern. Canadian businessmen can cite chapter and verse to verify its validity. During my

¹⁸The Conference Board of Canada, Study No.81: "A fit place for investment?", by Duncan McDowall, April 1984.

experience on boards of directors in the private sector, I have encountered several instances in which decisions about where to locate a new plant have been taken on exactly these grounds... when locational decisions are made contrary to strict market considerations, it is not unreasonable to expect that the larger market will be favored as a safer haven."¹⁹

More specifically, this uncertainty tends to affect adversely both shorter-term production and longer-term investment decisions of Canadian-based companies presently exporting to the U.S. As well, U.S. trade remedy laws may have negative effects on the export decisions of those Canadian-based companies which are not presently exporting to the U.S., or have just recently entered that market.

A further potential economic impact of U.S. trade remedy laws on Canada is the detrimental effect which such targeted U.S. protection might have on the investment decisions of foreign companies -- both U.S. and offshore -- to either newly invest, or expand present production capacity in Canada. Of concern in this regard is the fact that two recent U.S. AD cases against Japanese exports have also cited exports from the successful subsidiaries in Canada. -- Mitsubishi (colour picture tubes) and Kao-Didak (computer micro-diskettes).

The uncertainty of less than secure U.S. market access, generated by active use of U.S. trade remedy laws by American producers, can influence key investment decisions to invest in Canada by domestic and foreign companies as they attempt to respond to U.S. competition.

¹⁹Simon Reisman, The Issue of Free Trade, from an article presented at U.S.-Canadian Economic Relations: Next Steps?, a conference by the Brookings Institute, Washington D.C., 1984, and partially reproduced in The Free Trade Papers, edited by Duncan Cameron, Toronto, 1986.

IV IMPLICATIONS OF THE PROPOSED CANADA-U.S. AGREEMENT

The Government of Canada initiated discussions with the U.S. in order to achieve three key objectives in relation to U.S. market access.²⁰ First, the Federal Government sought to expand or "enhance" Canadian market access through the elimination of U.S. tariffs (of interest to Canadian exporters of products such as petrochemicals and footwear), quotas and other NTBs, and more importantly through improved access into U.S. federal and state government procurement markets.

Second, one of Canada's chief objectives was to "secure" market access by establishing a reciprocal exemption from the application of trade remedy measures between the two countries. Instead there would be disciplines with respect to government support programs which would make CVD laws against subsidies redundant. AD laws would be replaced by domestic competition policy measures maintained by the two countries to address price discrimination. In addition, Canada sought exemption from U.S. Sec.301 and Sec.337 laws (unfair trade practices) as applied to Canada.

And third, the Canadian government sought to "enshrine" our enhanced and secured market access through "a strong dispute settlement mechanism to reduce the disparities in size and power and to provide fair, expeditious and conclusive solutions to differences in view and practice."

A. The Outcome of Negotiations

1. Enhanced Market Access

In the area of enhanced market access, the Agreement clearly achieves bilateral tariff elimination. However, since Canada has substantially higher tariffs and a smaller domestic market than the U.S., Canada would face the bulk of the transitional industrial adjustments which occur as a result of tariff elimination.

In terms of achieving greater access into U.S. government procurement markets, the Agreement appears to achieve only limited success. The Canadian federal government has indicated that of the approximately \$750 billion (Cdn.) of annual expenditures

²⁰Source: External Affairs Canada, Canadian Trade Negotiations: Introduction, Selected Documents, Further Reading, 1986, pp. 3-4.

by all U.S. governments -- nearly twice Canada's GNP -- the Agreement provides for increased access opportunities for Canadian suppliers to less than \$3.2 billion (Cdn.) of that market, or less than 0.5% of total U.S. government expenditures.

A number of Canadian industries, such as steel, urban transportation and power generation and transmission equipment manufacturers have long been interested in achieving greater access into U.S. government procurement markets. The procurement provisions of the Agreement, however, appear to provide little new U.S. market access in these areas.

2. Secured Market Access

The benefits to Canadian producers from enhanced or increased U.S. market access that results from the Agreement are circumscribed unless Canadian exporters are effectively secured from the potential threat of U.S. trade remedy actions. The Agreement, however, does not appear to achieve a significant improvement in the security of Canada's market access into the U.S. Canada's vulnerability to U.S. trade remedy actions remains largely unaffected by the proposed Agreement. All U.S. trade remedy laws (AD, CVD, Sec.301, Sec.337, national security), with the exception of some changes to safeguards law, can still be brought to bear against Canadian exports as before the Agreement. Nor does the Agreement provide for improved market access for important Canadian exports such as softwood lumber, since the Memorandum of Understanding and the 15% Canadian export tax remain in effect.

Discussions on establishing new AD and CVD rules, including clearer definitions governing what is a permissible government financial assistance program, resulted only in agreement to undertake further negotiations over a maximum of seven years.

AD/CVD Dispute Panel

Both countries' AD and CVD laws remain in place and would continue to be enforced as they presently are by their respective domestic administering authorities. The principal departure from present practice is that a final AD or CVD decision from a country's domestic administrative process can be appealed by the other party to the binational AD/CVD dispute settlement Panel. However, these AD/CVD Panels are only permitted to review decisions that the administering authority has made, in order to ensure consistency with the law and precedent of that country.

For Canada, this new binational Panel for AD and CVD cases does not appear to represent a significant improvement over the previous appeal procedure to the U.S. Court of International Trade (CIT). The AD/CVD Panel in effect replaces the CIT, since its review mandate would be the same. Yet there appears to be little evidence to indicate Canadian corporate dissatisfaction with the CIT itself. In fact, the Canadian softwood lumber industry appeared to be willing to have the 1986 U.S. CVD investigation run its course, and seek a CIT review in case of a positive final determination by the U.S. administering authorities.

The reviewing standard which the CIT presently follows -- and which will be followed by the AD/CVD Panel -- is that it must accept a decision by the administering authority concerned (e.g., the U.S. Department of Commerce), if the record of investigation in the case contains "substantial evidence" to support that decision, and the decision is consistent with U.S. law. As such, and with respect to decisions of both the CIT and AD/CVD Panels:

"This is not a very demanding standard to satisfy, and U.S. administrators will continue to possess broad discretion to apply existing U.S. law in ways that will hinder Canadian exporters by creating costly barriers to entry through AD/CV duty litigation."²¹

Furthermore, it can be argued that the bulk of the problems for Canadian exporters caught up by U.S. AD or CVD investigations is caused by the exercise of administrative discretion at the preliminary stages of AD/CVD proceedings. This is particularly true given that the U.S. AD and CVD administrative processes require little evidence to initiate an investigation, and that the preliminary test of injury can be easily met.²² Thus, even when a U.S. petition is eventually dismissed at the administrative stage, or reversed by an appeal Court or an AD/CVD Panel, Canadian exporters affected would nevertheless face the harassment and costs of the investigation for a number of months.

Reducing the value of AD/CVD Panels is the fact that U.S. trade laws provide

²¹Quinn, *op.cit.*, p. 8.

²²These biases against the exporter in U.S. AD and CVD investigations at the preliminary stage are documented in Alan M. Rugman, U.S. Protectionism and Canadian Trade Policy, Journal of World Trade Law, Vol.20 No.4, 1986.

administrators a high degree of judgemental discretion, and the standard for review is limited. Furthermore, the Panels are not empowered to review cases in terms of their consistency with GATT, but rather with respect to their consistency with U.S. law. As such, U.S. AD/CVD law encourages the filing of legally spurious complaints:

"...by failing to provide any concrete definition of the types of foreign government programs which can be challenged as countervailable subsidies... Binational panels will be constrained to recognize that U.S. administrators have been authorized by Congress to exercise broad discretion since their review will be limited to questions of compliance with U.S. law."²³

In this regard it is also important to note that precedents established in U.S. cases against other countries could be used by the AD/CVD Panel in interpreting the application of U.S. law against Canadian producers. Any increasing protectionism of the Department of Commerce is therefore unlikely to be easier to overturn.

A further difficulty could arise in a situation where, for example, a U.S. CVD or AD investigation against similar products from several countries, including Canada, could be appealed to both the CIT (products from other countries) and the Panel (Canadian products). This situation could lead to questions of paramountcy between the two appeal processes in terms of precedent, and raises questions about the workability of the Panel procedure.

A final concern with the AD/CVD binational Panel system flows from the fact that panelists will be chosen on an ad hoc, case-by-case basis rather than appointed for fixed terms. It is not unlikely that this method of selecting panelists might lead individual members to be cognizant of their government's interests in the particular case, especially if it is one with particularly sensitive implications (e.g. softwood lumber). Individual panelists may also be more deferential to the administrative interpretation of AD/CVD law, rather than develop a broad vision of the Agreement's objectives as may be possible with a more permanent body.

One significant improvement that the AD/CVD Panel review process would have over the present system is that Panels would be required to reach a ruling within 315 days, which is considerably faster than is common for a comparable U.S. Court review.

²³Quinn, *op cit.*, pp. 9-10.

However, increased speed at the conclusion of an investigation cannot offset the cost, harassment and trade and investment dampening effects on Canadian producers of defending a case through the administering authorities in the U.S.

Moreover, there would appear to be little likelihood that the potential for review by a binational Panel of an affirmative final AD/CVD determination, with all its associated investigation and legal expenses to the exporter, could significantly deter U.S. industries from filing marginal AD/CVD petitions.

"Therefore, discretionary judgements at the preliminary stages of the proceeding will be virtually unreviewable, and it is these administrative decisions which have contributed most importantly to the creation of incentives for U.S. industries to employ AD/CV duty actions as an anti-competitive strategy for imposing costs on their foreign competitors."²⁴

While there is the potential that the impartial nature of the binational AD/CVD Panels and their decisions might tend to reduce the number of investigations initiated on legally insufficient cases, in practice this might not be the case.

"Since binational panels will apply U.S. law, and employ the same permissive standards for review as U.S. courts, there is no rational basis for expecting any material improvements in the administration of U.S. AD/CV duty law as a result of the Agreement."²⁵

Restriction on Changes to CVD/AD Law

Chapter 19 of the Agreement also provides that any statutory changes to AD/CVD laws do not apply to the other Party unless the legislation specifically provides for it, and that such changes must be consistent with the "objects and purposes of the Agreement". This could provide Canada with a de facto exemption from future U.S. statutory changes to AD/CVD laws (i.e., post January 1, 1989) which are written so as to broadly target U.S. imports.

²⁴Ibid, p. 12

²⁵Ibid, p. 13

However, this provision would not be effective in constraining a protectionist U.S. Congress intent on implementing changes to AD and CVD laws for the benefit of particular U.S. industrial interests. In fact, a protectionist Congress could argue that a proposed reform to U.S. AD/CVD law is needed to secure a "level playing field" and to prevent further injury to U.S. firms from "unfairly traded imports". As such, the particular reform could be considered to meet a declared objective of the Agreement, that of ensuring "effective disciplines on unfair trade practices".

In view of this possibility, it would appear that U.S. GATT obligations will be the only effective means of constraining any future changes to U.S. AD and CVD laws. However, the Agreement does not address the issue of whether the AD/CVD Panel would be the authoritative determinator of GATT law for the purposes of the Agreement.

Nor is the effectiveness of this provision against further trade restricting changes in U.S. AD/CVD laws clear. In cases where a bilateral Panel found against proposed changes in U.S. AD/CVD law, enforcement in the absence of U.S. compliance could not be ensured, given that abrogation of the Agreement by Canada or the enactment of comparable legislation are Canada's only options.

Relation to U.S. Omnibus Trade Bill

Canada was not exempted from the U.S. Omnibus Trade Bill which was recently passed by the U.S. Congress. This Bill, if enacted into law, would change U.S. trade laws in a number of key areas which could negatively impact on Canadian exports. These areas include:

- i) the widening of the U.S. definition of a countervailable subsidy. Unless the standstill commitments of the Canada-U.S. Agreement are recognized, the Agreement itself would not protect Canada against any of the provisions amending U.S. AD and CVD law (e.g. codification of the "generally available" definition used in the 1986 softwood lumber case). The additional provision for investigation of investment barriers in industries receiving subsidies could possibly be worrying for the Canadian fishery and mining sectors.
- ii) an expansion of the list of foreign trade practices that would be actionable under Sec.301 (e.g. "export targetting"). The provisions limit Presidential discretion and tighten definitions of unfair practices. This would encourage the Administration to initiate Sec.301 actions more frequently and give private

parties greater power to compel action. Specifically, the inclusion of "export targetting" as an unfair practice could be used against a wide variety of Canadian industrial development programs.

- iii) the removal of the injury test requirement from Sec.337 investigations. The Omnibus Bill provisions on Sec.337 significantly strengthen present legislation. With the removal of the need to show that the U.S. industry has been injured, the likelihood of actions and success of actions against Canadian exports would likely increase.
- iv) the allowance for cumulation in safeguards cases. The Omnibus Bill provisions on safeguards could make injury findings more likely, particularly during a recession. The Agreement will not protect Canada from this increased risk if Canada contributes a significant share (over 5%) of U.S. imports.
- v) the potential for increased use of U.S. national security laws. Omnibus Bill amendments to U.S. Sec.232 laws could lead to an increased use of this trade remedy if other actions are unlikely to be successful.

The December 8, 1987 Report of the all-party House of Commons Standing Committee on the Elements of the Agreement, concluded that the Omnibus Trade Bill would impair the benefits to Canada under the Free Trade Agreement, and recommended that "...the government should withdraw its consent from the Agreement - unless Canada is formally exempted from the application of this U.S. legislation."

Many proponents of the proposed Canada-U.S. Trade Agreement have argued that the Agreement would create a special trading relationship between the two countries. The fact that Canada was not exempted by the U.S. Congress from the provisions of the Omnibus Trade Bill suggest that such a special relationship has not been achieved as a result of the Trade Agreement.

Safeguards

The Agreement did achieve new rules, and a degree of exemption for Canada, in the application of U.S. safeguard laws. Canadian goods would be exempt from the general application of a safeguard measure against all U.S. imports when Canada's share of

U.S. imports is not considered to be substantial (i.e., normally less than 5% to 10%).²⁶

Early indications are that the changes to the global application of U.S. safeguard law could work to reduce sideswiping instances affecting Canadian exports, and that a degree of market access would be maintained even when Canada is a substantial exporter. These potential benefits must be tempered, however, with the recognition that these new rules would not have prevented the 1986 imposition of duties on Canadian shakes and shingles exports to the U.S., nor would they reduce in any significant way the difficulties the Canadian steel industry has encountered since 1983 in exporting to the U.S. For the Canadian steel industry, the safeguard provisions would only retain recent levels of U.S. market share plus levels of growth in that market, rather than allow currently competitive Canadian-based steel firms from increasing their levels of market penetration in the U.S.

As well, the Agreement allows for either the re-imposition, or postponement of the tariff reduction schedule during the ten year tariff elimination transition period, if such tariff reductions result in import surges that cause serious injury. This could prove to be valuable to the less competitive Canadian industries that might experience substantial adjustment and restructuring difficulties.

3. Enshrined Market Access

In order to enshrine any gains in U.S. market access, a set of strong institutional provisions would be required to deal with disputes over the interpretation and workings of the Agreement's substantive provisions other than those in respect of AD/CVD laws.

The Agreement proposes a GATT-like process of consultation, mediation, arbitration, fact-finding and attempted resolution by consensus.

If the Canada-U.S. Trade Commission established by the Agreement cannot jointly agree on a decision, or the findings of an arbitration Panel are not implemented,

²⁶However, even when Canada's exports are considered to be substantial, there is some market access protection for Canada in that the volume of exports may not be allowed to be reduced below the trend of exports over a "reasonable" recent base period, with some allowance for growth in those exports.

then the aggrieved party may retaliate. However, retaliation as a means of enforcement does not adequately offset the disparities in political and economic strengths which are inherent in Canada's economic relationship with the U.S.

Whether the Commission is an improvement over existing international arrangements is yet uncertain. A leading GATT authority²⁷ has recently argued that the lack of a permanent bilateral secretariat associated with the Commission, unlike in the present GATT system, could seriously undermine the efficacy and quality of Panel decisions.

A further concern is the critical issue of provincial involvement in the dispute settlement mechanism. Such involvement would appear to be essential whenever any dispute involves: provincial legislation; programs or policies or any matter of provincial constitutional ability; whenever any dispute involves a matter of shared constitutional responsibility; or whenever the matter, although under federal jurisdiction, has a significant impact on the provinces.

However, provincial involvement under such circumstances is not provided as a right in the Canada-U.S. Trade Agreement. To the extent that provisions are made for provincial involvement, this would appear to be largely at the discretion of the federal government. The situation may therefore arise where provincial policy areas, such as in services or investment, could be subject to dispute, and the provinces would have to rely on the federal government (as the Party to the Agreement) to determine whether and how to defend these policies before a dispute Panel.

B. Canadian Adjustment Strategies

As a result of the rapidly changing structure of world trade and production, as well as the Canada-U.S. Agreement, Canadian firms will need to meet a level of investment that would allow for:

- i) expansion of basic domestic production capacity to supply general U.S. and other foreign markets, as well as the more specific identification and exploitation of rapidly growing niche markets.

²⁷Robert Hudec, presentation to the University of Ottawa Conference on the Canada-U.S. Free Trade Agreement, January 22, 1988.

- ii) maintaining longer-term profitable operations of multinational enterprises with subsidiaries in Canada with, for example, a narrower product-range mandate, as head offices balance the costs and benefits of relocating to centralized locations in the U.S.
- iii) further exploitation of Canada's comparative advantage on a wide range of natural resource exports.

The structural economic and regional differences between Canada and the U.S., along with significantly differing philosophies as to what role government should and needs to play in domestic economic development, have served as a background to, and historically justified, a higher level of government involvement in Canada's economy. On the other hand, the U.S. defence budget has long been utilized by the U.S. government as an important and effective tool for achieving R&D as well as industrial and regional development goals in the U.S. economy.

These inherent differences in the structures and dynamics of the Canadian and American economies dictate that a "Canadian" economic development or adjustment strategy will need to be significantly different from an "American" approach. Given these realities, the inability of the Canada-U.S. negotiations to, for example, reach new definitions on what constitutes countervailable government programs maintains the vulnerability of Canadian adjustment strategies that aim to address the domestic restructuring required by global competition.

C. Continued Canadian Vulnerability to U.S. Trade Actions

1. Trade Actions by Uncompetitive U.S. Industries

The Agreement entails little significant improvement in security of access for Canadian exporters to the U.S. market. The principal threat to Canadian access to the U.S. market, namely the range of U.S. trade remedy laws, are not effectively controlled. For most U.S. trade laws, the Agreement provides neither new standards to govern such trade actions, nor any effective method for preventing their use to both harass and limit competitive Canadian exports.

An example of how market access for competitive Canadian industries can be countered, is the possibility of a trade action against Canadian zinc exports to the U.S. Zinc alloy imports into the U.S. face import tariffs of as high as 19%. The

U.S. zinc mining industry has previously considered filing a CVD petition against their Canadian competitors. The increased competition resulting from tariff-free zinc imports from Canada may well induce the U.S. industry to file a CVD or safeguards petition. The provisions in the Agreement offer little protection for Canada against such an action.

Appendix E attempts to identify U.S. manufacturing and resource-based industries which would face increased competitive pressure from either Canadian exporters under the Agreement, or third country exporters in the short to mid-term. The more uncompetitive U.S. industries, which are also the strongest opponents to the Agreement, are the most likely to employ U.S. trade remedy laws in order to counter the market access that Canadian producers are able to achieve under the Agreement.

For example, the U.S. uranium, plywood, non-ferrous metal (e.g., copper, lead and zinc), coal, electricity and oil and natural gas industries are attempting to influence U.S. implementing legislation for the Agreement, while also threatening to use the wide range of U.S. trade laws against Canadian exports.

As well, there are strong U.S. agricultural interests opposed to the Agreement who have recently, as in the past, targetted as unfair subsidies various domestic government financial assistance programs to Canada's farm sector. U.S. Congressional backers of these American agricultural interests have suggested that implementing legislation for the Agreement should require the U.S. Administration to self-initiate CVD and Sec.301 trade actions against these Canadian agricultural assistance programs.

Further opposition to the Agreement comes from U.S. steel interests which are seeking to further curtail Canadian access through a variety of measures.

In summary, U.S. opposition to the Agreement is sharpest in American industries where Canadian producers are competitive (e.g., steel products), hold a comparative advantage (e.g., natural resources) or where particular Canadian practices are perceived by the U.S. as unfair (e.g., agricultural products). The ability of Canadian producers to benefit from increased U.S. market access, or to rationalize to better compete in the Canadian market, could be severely restricted by both the threat, or actual use, of a variety of U.S. trade remedy laws, which remain largely unrestricted under the terms of the Agreement.

2. U.S. Trade Actions in Response to Canadian Adjustment

The Canadian federal government, in its strategy to negotiate a trade deal with the U.S., implicitly assumed that there would be a sufficient pool of investment capital available to Canadian firms to undertake the needed industrial adjustment, and that firms' responses to the Agreement would be such that all the correct and needed decisions to reap the benefits of increased U.S. market access would occur.

However, it is precisely these same Canadian industries that, by becoming more competitive and thus experiencing substantial export success in the U.S., would at the same time be potentially the most vulnerable to U.S. trade remedy actions from their U.S.-based competitors. Table 3 lists a number of such potentially successful Canadian industries previously identified by various free trade studies (including Federal and Ontario government analyses).

TABLE 4²⁸
CANADIAN INDUSTRIES IDENTIFIED TO EXPERIENCE
EXPORT GAINS IN THE U.S. AS A RESULT OF THE AGREEMENT

<u>Resource-based Industries:</u>	
- non-ferrous metals	- exterior wood-based panels
- pulp and paper	- petrochemicals
- uranium	- fishery products
 <u>Manufacturing Industries:</u>	
- distilleries	- forest harvesting machinery
- instrumentation	- environmental equipment
- steel mill products	- telecommunications equipment
- railroad equipment	
- electrical power generating equipment	

While these Canadian industries have been identified as indicative of those industries which would potentially benefit from the Agreement through increased

²⁸Appendix E identifies corresponding U.S. industries experiencing competitive difficulties.

exports to the U.S. market, their particular competitive strategies in further penetrating the American market would continue to be vulnerable to U.S. trade remedy actions.

For example, competitive pricing strategies employed by Canadian-based manufacturing companies exporting into the U.S. could be considered to be dumping strategies by the U.S. Such a pricing strategy would arise as Canadian firms, while maintaining some protection behind tariffs in the transition period, price competitively in the U.S. market in order to increase exports in preparation for full tariff-free trade.

Furthermore, failure to obtain the initial goal of new rules governing U.S. CVD trade remedies would maintain the present vulnerability of a wide range of Canadian government industrial assistance programs. These are programs which, for some industries, may be required in order to facilitate or complement their corporate adjustment strategies to deal with the requirements of the Agreement and ongoing increases in international competition.

Therefore, U.S. trade remedy laws might very well reduce substantially the potential export gains to Canada identified to result from any increased U.S. market access due to the elimination of U.S. tariffs, and may significantly threaten Canadian firms' adjustment strategies. As well, ongoing market access threats to Canadian exports by U.S. industries presently experiencing competitive difficulties in their domestic market would not be curtailed.

V NEGOTIATIONS ON NEW CVD/AD LAWS

The development and establishment of a new regime that would govern the use of bilateral trade remedy laws was identified by Canada as a fundamental requirement in achieving a successful outcome to the negotiations with the U.S.

A recent article by a senior federal government official identified the main features of an ideal regime.²⁹ Both countries would:

- determine jointly what would constitute an offensive trade distorting practice;
- agree not to engage in such subsidy practices (i.e., offensive trade distorting) and accept greater discipline on other forms of subsidy practices;
- address trade distorting private practices (e.g., dumping and copyright infringement) under domestic laws and procedures of general application (e.g., domestic competition and patents legislation);
- establish effective disciplines to govern measures dealing with import surges (i.e., safeguards);
- enter into new obligations to notify, consult and if necessary, trigger dispute settlement procedures;
- and limit to the extent practicable, border remedies to deal with the remaining practices (e.g., Sec.301 and Sec.232).

The outcome of the negotiations, however, was a bilateral agreement that fell short in addressing the main features of Canada's key objective.

A principal shortfall of the Agreement is that it does not restrict the use by U.S. industries of Sec.301 and Sec.337 actions. But more importantly, U.S. CVD and AD trade laws remain in place, with only the understanding that both countries would

²⁹Hart, op.cit., p. 288.

undertake, over a maximum of the next seven years, further negotiations towards a common bilateral code to govern CVD and AD investigations.

A. Failure of Subsidy/CVD and AD Negotiations

There are several factors that can be identified to have served as key stumbling blocks and which, more importantly, are likely to remain serious impediments in future discussions.

For example, it is apparent that the U.S. Congress was not willing to accept a curtailment of present American industry defences against "unfair" trade. This reluctance to forego protective remedies available to domestic producers is likely to remain.

Furthermore, both sides strongly disagreed on how to approach a common set of rules. While Canadian negotiators were aiming at an agreement over a set of new and clearer rules that would require further disciplines on subsidies, thus making CVD redundant, U.S. negotiators were more interested in identifying those current Canadian programs that in their view should be curtailed.

However, the U.S. side appeared unwilling to match its demand for increased disciplines over the use of Canadian provincial practices -- along with federal practices -- with a similar commitment to ensure the disciplining of U.S. State practices. Failure to ensure this would have created a highly unbalanced arrangement, leading to distortions in North American production, investment and employment to the benefit of the U.S. economy.

As well, the U.S. side appeared to have difficulty in accepting Canada's requirement that it should be able to maintain a regional development assistance capability, and was apparently unwilling to fully recognize the need for differing industrial policies in Canada vis-a-vis the U.S. approach to government assisted domestic economic development, which to a large degree flows from U.S. defence expenditures.

B. Likelihood of Future Success

The prospect of future negotiations on subsidies raises a host of concerns that revolve around Canada's future ability to establish and carry out a unique, made-in-Canada industrial and regional development strategy. Even the determination

of what constitutes a "countervailable" or "trade distorting" subsidy involves difficult debate about the role of government, and the use of different policy tools to achieve economic and social objectives.

At the industry level, there are also a number of concerns associated with these planned future negotiations. As a recent monthly bulletin by Clarkson Gordon/Woods Gordon noted:

"the uncertainties posed by these extended talks could delay the investment expenditures that free trade is intended to promote in Canada, thereby postponing the expected stimulus to incomes and employment. To the extent that businesses do proceed with restructuring, Canada's negotiating position will be weakened as the years pass by the fact that economic adjustments to free trade will be too far along for us to credibly threaten to back out of the deal."³⁰

While a number of factors worked to prevent success in achieving a new set of CVD and AD rules over the 18 months of the negotiations, the extended schedule for further bilateral negotiations in this area does not necessarily increase the likelihood of future success. In particular, the longstanding unwillingness by the U.S. Congress to surrender its present and future control over U.S. trade law would likely make successful negotiations difficult.

Negotiators may propose the replacement of AD trade laws with domestic competition legislation. Given that Canada has shown a greater propensity to activate AD investigations against the U.S., replacement of current AD trade laws should be seen as a Canadian concession.

Moreover, there are potentially serious concerns surrounding the adequacy of using Canadian competition law as a replacement for domestic AD trade law. It is generally recognized that there are substantial differences between American and Canadian competition laws. Removal of AD trade law could place Canadian-based firms at a disadvantage vis-a-vis American-based firms because, for example, the burden of proof required to establish price discrimination³¹ is much greater in Canada, and

³⁰Business Conditions, January 1988, prepared by the Marketing and Economics Group of Woods Gordon.

³¹The corollary of "dumping" in domestic competition policies.

the rights of private legal action to Canadian courts are more restricted.

To achieve new rules governing CVD actions, it is likely that Canada would need to make further concessions to the U.S. These further concessions could be either within the set of issues to be negotiated -- such as substantial disciplines in the use of assistance programs by Canadian governments -- or concessions on issues totally unrelated to these negotiations, such as disciplines on the behaviour of Canadian government monopolies.

Moreover, there is little evidence to-date that the U.S. would be prepared to recognize that the differing economic structures of the two countries require different approaches in government assistance strategies. There is a very real danger that Canada would be forced to depend on an approach to economic development similar to that of the U.S. It is questionable whether such an approach to economic development would recognize the unique structure of the Canadian economy.

VI CONCLUSION

For Canadian-based companies the increased level of access into the U.S. market resulting from the Canada-U.S. Trade Agreement would largely be due to U.S. tariff elimination. The potential economic benefits from this increased level of access, however, would be circumscribed if gains in access are countered through trade remedy actions that prevent Canadian industries from competing effectively in the U.S. market.

The Canada-U.S. Trade Agreement, however, falls short of securing Canada's access into the United States. American industries would continue to have complete access to the wide range of U.S. trade remedy laws which remain in place essentially as currently written. The U.S. administering authorities, such as the U.S. Department of Commerce and the International Trade Commission, are not affected by the Agreement in how they interpret these laws and determine legal precedents. These two bodies have investigated in total well over 600 anti-dumping and countervailing duty cases from 1980 to 1986. The continuing use of these laws by America's businesses is a strong acknowledgment of their effectiveness.

This inherent lack of security in U.S. market access could render vulnerable the competitive strategies of Canadian-based firms seeking to either enter or expand into U.S. markets as a result of U.S. tariff elimination. As well, government financial assistance programs aimed at facilitating and advancing the required transitional adjustment process would continue to be vulnerable.

The inability of the negotiations to achieve meaningfully different treatment for Canada under U.S. trade remedy laws, implies not only that Canada would remain vulnerable to U.S. trade actions arising from current U.S. trade laws, but also vulnerable to present or future proposed changes to these laws. Many provisions in the U.S. Omnibus Trade Bill, the future of which is still uncertain, would work to rewrite in a more protectionist tone the range of American trade laws. The bilateral Agreement with the U.S. would not prevent these changes from affecting Canada.

Canada did not meaningfully achieve its key objective of secure access to the U.S. market. To the extent that improved access was negotiated in terms of U.S. tariff reduction (although not in access to U.S. government procurement), these benefits may not be fully realized if producers do not choose to expand investment in Canada to export to the U.S. The continued use of U.S. trade laws may be an important determinant in a firm's decision to either establish new, or expand present production capacity in Canada in a tariff-free environment, and is therefore key in any assessment of the value of the agreement.

The fact that the Agreement as signed on January 2, 1988, does not substantively change bilateral trade remedy laws should be seen as a significant shortcoming of the Agreement in balancing the overall gains and concessions in the broader Canada-U.S. trade negotiations.

APPENDIX A

Table A-1
CANADIAN MERCHANDISE EXPORTS BY DESTINATION
SELECTED YEARS % OF TOTAL

COUNTRY/REGION	1966	1970	1974	1978	1982	1984	1986
U.S.	59.85	64.7	65.54	70.21	68.16	75.5	77.5
JAPAN	3.91	4.9	7.03	5.87	5.59	5.2	5.1
U.K.	11.14	8.9	6.03	3.82	3.26	2.2	2.2
OTHER EEC	7.09	8.0	7.37	5.91	6.18	4.2	4.5
OTHER OECD	3.61	3.3	2.91	1.82	2.13	1.7	1.7
TOTAL OF ABOVE	85.61	89.8	88.90	87.65	85.34	88.8	90.9
REST OF WORLD	14.38	10.2	11.09	12.34	14.65	11.2	9.1
WORLD TOTAL	100.00	100.0	100.00	100.00	100.00	100.0	100.0

Source: Statistics Canada

Note: EEC & OECD figures are for membership as defined in 1988.

Table A-2
CANADIAN EXPORTS TO THE U.S. 1978 - 1986
(Millions of \$'s)

1978	37,002.7
1979	44,454.0
1980	48,062.2
1981	55,432.5
1982	57,501.6
1983	66,332.5
1984	85,055.6
1985	92,968.1
1986	93,170.2
1987	94,561.2*

Source: M.I.T.T.: Canadian Trade by Country,
Historical Summary, 1978 - 1986
* Statistics Canada

Table A-3
RELATIVE VALUE OF EXPORTS TO GNP

1986	Canada (\$Cdn.)	Japan (Yen)	U.S. (\$U.S.)
GNP	\$493.01 bn.	330,752 bn.	\$4,235 bn.
EXPORTS	138.06 bn.	43,428 bn.	290.1 bn.
EXPORTS%GNP	28%	13.13%	6.85%

Source: International Financial Statistics

U.S. CVD ACTIONS AFFECTING CANADA

Year	Product	Preliminary Injury	Preliminary Subsidy	Final Subsidy	Final Injury	Final Disposition
1980	Frozen Potato Products	Negative	-	-	-	Case terminated
1980	Unprepared Fish	Affirmative	Affirmative	Affirmative	Negative	Case terminated
1980	Potassium Chloride	Negative	-	-	-	Case terminated
1981	Hard Smoked Herring and Fillets	Negative	-	-	-	Case terminated
1982	Certain Rail Passenger Cars (Bombardier)	Affirmative	Affirmative	Affirmative	-	Petition withdrawn Case terminated
1982-83	Softwood Lumber	Affirmative	Negative	Negative	-	"De Minimus" final subsidy determination
1984-85	Hogs and Pork	Affirmative	Affirmative	Affirmative	Affirmative-hogs Negative-pork	CVD order issued covering hogs
1985	Raspberries (B.C.)	Affirmative	Affirmative	-	-	Suspension agreement signed
1985	Iron and Steel Pipes and Tubes	Affirmative	Negative	Negative	-	Case Terminated
1985-86	Fresh Atlantic Ground-fish	Affirmative	Affirmative	Affirmative	Affirmative	CVD order issued
1985-86	Oil Country Tubular Goods	Affirmative	Affirmative	Affirmative	Affirmative	CVD order issued
1986	Softwood Lumber	Affirmative	Affirmative	-	-	Memorandum of Understanding signed
1986	Cut Flowers	Affirmative	Affirmative	Affirmative	Affirm.-standard Negat.-miniature	CVD order issued on standard

U.S. ANTIDUMPING INVESTIGATIONS AGAINST CANADIAN PRODUCERS

Year	Product	Preliminary Injury	Preliminary Dumping	Final Dumping	Final Injury	Final Disposition
1981	Asphalt Roofing Shingles Canned Clams	Negative Negative	- -	- -	- -	Case terminated Case terminated
1982	Sugars and Syrups Sheet Piling Chlorine Frozen French Fries	Affirmative Affirmative Negative Negative	Affirmative Affirmative - -	Affirmative - - -	Affirmative - - -	A/D order issued Price undertaking Case terminated Case terminated
1983	Certain Fresh Potatoes	Affirmative	Affirmative	Affirmative	Negative	Case terminated
1984	Choline Chloride	Affirmative	Affirmative	Affirmative	Affirmative	A/D order issued
1985	Rectangular Steel Tubes & Pipes Salted Cod Fish Rock Salt Egg Filler Flats Iron Construction Castings Raspberries Oil Country Tubular Goods	Affirmative Affirmative Affirmative Affirmative Affirmative Affirmative Affirmative	Affirmative Affirmative Affirmative Affirmative Affirmative Affirmative Affirmative	Affirmative Affirmative Affirmative Affirmative Affirmative Affirmative Affirmative	Negative Affirmative Negative Negative Negative Affirmative Affirmative	Case terminated A/D order issued Case terminated Case terminated A/D order issued A/D order issued A/D order issued
1986	Brass Sheet & Strip Fresh Cut Flowers	Affirmative Affirmative	Affirmative Affirmative	Affirmative Affirmative	Affirmative Affirmative	A/D order issued A/D order issued
1987	Picture Tubes Potassium Chloride	Affirmative Affirmative	Affirmative Affirmative	Affirmative Affirmative	Affirmative -	A/D order issued Price Undertaking
1988	Computer Microdisks	Affirmative	-	-	-	-

ONTARIO COMPANIES INITIATING ANTIDUMPING INVESTIGATIONS AGAINST U.S. COMPANIES

Ontario Company	Location	Product	Initiation Date	Status
Gendron Industries Ltd. Jolly Jumper Inc.	Toronto Cambridge	Juvenile Products	23/06/80	Case rescinded
Sherman Supersonic Industries (Canada) Ltd. Wash World Industries	Mississauga Mississauga	Vehicle Washing Equipment	07/07/80	A/D order issued
Penwalt of Canada Ltd.	Oakville	Benzoyl Peroxide	18/08/80	Negative No injury
Notting Canada Inc.	Mississauga	Standard Cutting and Creasing Steel Ruler	14/09/81	A/D order issued
Do-Tan Manufacturing Ltd.	Dundas	Industrial Wood Cutting Band Saw Blades	09/07/82	A/D order issued
Moldex Ltd.	Barrie	Toilet Seats	22/09/82	Case terminated
Allied Chemicals	Mississauga	Soda Ash	16/12/82	A/D order issued
Trans-Canada Contact Lens Ltd.	Toronto	Contact Lenses	04/02/83	Negative No injury
Associated Tube Industries Ltd.	Markham	Stainless Steel, Nickel & Nickel Alloy Pipe	20/06/83	A/D order issued
Nixon Plate Coils Ltd.	Gormley	Plate Coils	08/06/83	A/D order issued
The Canadian Sugar Institute	Toronto	Sugar	24/10/83	Negative No injury
Duraform Concrete Systems Ltd.	Mississauga	Plywood Concrete Forming Panels 1-1/8 in.	04/10/84	Case terminated
Canadian Porcelain Company Ltd.	Hamilton	Porcelain Insulators	09/01/85	A/D order issued
Xytel Energy Ltd.	Burlington	Automated plants	14/02/85	Negative No dumping

UNITED STATES' SAFEGUARD RECORD

APPENDIX D

<u>Year</u>	<u>Sector</u>	<u>Commodity</u>	<u>Relief</u>	Potential Ontario <u>Trade Impact</u> \$	<u>Target</u>
1980	Fish	Fish	None	\$0	Sideswipe
1980	Agriculture	Mushrooms	Duties 3 Yrs.	\$15-18 m.	Sideswipe
1980	Manufactures	Certain Motor Vehicles	None	\$5.11 b.	Sideswipe
1980	Apparel	Leather Wearing Apparel	None	\$2.8 m.	Sideswipe
1984	Semi-Manufactures	Specialty Steel Stainless/Alloy	Duties 4 Yrs. Quota 4 Yrs.	\$14-20 m.	Sideswipe
1983	Semi-Manufactures	Carbon Steel	VRA (CDN Exclusion)	\$1.0 b.	Sideswipe
1984	Metals	Unwrought Copper	None	N/A	Sideswipe
1985	Agriculture	Apple Juice	None	\$2.0 m.	Sideswipe
1985	Agriculture	Sugar Blends	Quota 3 Yrs.	\$40-50 m.	Sideswipe
1985	Manufactures	Metal Castings	None	N/A	Sideswipe
1985	Manufactures	Fork Lift Arms	None	\$15.2 m.	Direct
1985	Semi-Processed Natural Resource	Shingles & Shakes	Duties 5 Yrs.	\$0	Direct
1985	Footwear	Non-Rubber Footwear	None	\$18.3 m.	Sideswipe

Key Features

- i) The U.S. record of relief award is modest, in only 5 of 13 petitions since 1980. However, the range of U.S. relief mechanisms used (duties, quota, VRA/QMA) and average duration of relief (4-5 years) far exceed Canadian experience. As well, the incidence of U.S. petitions, more than 3 times the Canadian rate increases the potential for harassment of Canadian producers and exports.
- ii) The U.S. has targetted Canadian product in only 2 cases since 1980 as the primary cause of U.S. injury. Of these, one was rejected (Fork Lift Arms 1985) and the other applied to a non-Ontario sector (Shingles and Shakes 1985).
- iii) In the one case since 1980 where a U.S. Voluntary Restraint Agreement (VRA) was applied under Safeguard law/Presidential discretion (Carbon Steel 1984), Canada negotiated an exemption on the basis of fair trader status. However, informal restraint by Canadian steel producers has significantly reduced Ontario exports from potential levels.
- iv) The U.S. has never been restricted in its requests for compensation, nor has it voluntarily excluded Canadian products from 3rd countries.

APPENDIX E

INDICATIVE LIST OF U.S. INDUSTRIES EXPERIENCING COMPETITIVE PRESSURE OR DECREASED DOMESTIC DEMAND

Manufacturing Industries

Telephone & Telegraph Equipment*
Electric Power Generating Equipment
Electrical Equipment
Machine Tools*
Steel Mill Products*
Footwear
Construction Materials
Railroad Equipment
Apparel
Dolls, Games & Toys
Jewelry
Silverware
Musical Instruments

Resource-Related Industries

Lumber & Wood Products*
Paper & Allied Products*
Crude Petroleum & Natural Gas*
Agricultural Chemicals
Primary Lead, Aluminum, Copper & Zinc
Coal Mining

* Indicates industries where Canada has been identified as potentially benefiting from increased exports to the United States under a Free Trade Agreement.

Sources: 1987 & 1988 U.S. Industrial Outlook, published by the U.S. Department of Commerce, Fortune Magazine, and Business Week.